GOVERNOR'S OFFICE OF BUDGET AND PROGRAM PLANNING

Fiscal Note 2013 Biennium

Bill #	SB0372	**Title:**	Lower business equipment tax -- phase more reduction on state economic growth
Primary Sponsor:	Tutvedt, Bruce	**Status:**	As Amended in Senate Committee

- ☑ Significant Local Gov Impact
- ☑ Needs to be included in HB 2
- ☑ Technical Concerns
- ☐ Included in the Executive Budget
- ☑ Significant Long-Term Impacts
- ☐ Dedicated Revenue Form Attached

FISCAL SUMMARY

	FY 2012 Difference	FY 2013 Difference	FY 2014 Difference	FY 2015 Difference
Expenditures:				
General Fund	$4,758,888	$13,091,639	$18,709,869	$18,905,437
Revenue:				
General Fund	($1,262,587)	($3,419,064)	($4,137,142)	($4,178,327)
State Special Revenue	($79,060)	($233,676)	($309,999)	($333,110)
Net Impact-General Fund Balance:	($6,021,475)	($16,510,703)	($22,847,011)	($23,083,764)

Description of fiscal impact: SB 372 provides for the reduction of the class 8 property tax rate from 3.0% to 2.0% for the first $2 million of market value of class 8 property owned by an individual or business. The $2 million tax bracket threshold is raised to $3 million and the tax rate is reduced to 1.5% the first tax year after corporation license and individual income tax collections exceed the prior year's collection by more than 4.0%, starting in FY 2012. All class 8 property above these thresholds would continue to pay the current law tax rate of 3.0%. The bill provides a means to reimburse local jurisdictions and the university system for 90% of the property tax base reduction experienced. The bill contains contingency language tying this bill to reimbursement mechanisms in, and passage of HB 26.

FISCAL ANALYSIS

Assumptions:

Department of Revenue (DOR)

1. The bill reduces the property tax rate from 3.0% to 2.0% for a tax bracket covering the first $2 million of class 8 (business equipment) taxable market value.
2. SB 372 provides for the reduction in the class 8 tax rate and raises the ceiling on the reduced tax rate bracket (threshold) the first time fiscal year corporate license tax and individual income tax collections exceed the

prior fiscal year's collections by more than 4.0%. Once this criterion is met, the class 8 rate is lowered to 1.5%, and threshold increased to $3 million.

3. All taxable market value above the bracket ceiling is taxed at the current statute taxable rate of 3.0%.
4. If HJR 2 revenue estimates for FY 2011, FY 2012, and FY 2013 are met, the bill's criterion for lowering the tax rate to 1.5% on the first $3 million of an individuals' or businesses' class 8 property would apply starting in TY 2013. This is presented in the following table:

HJR 2 Individual Income and Corp. License Tax Revenue Estimates under SB 372 as Amended "Trigger" Points. (millions $)

	Actual	HJR 2		
Source of Revenue	**FY 2010**	**FY 2011**	**FY 2012**	**FY 2013**
Individual Income Tax	$717.834	$738.761	$781.891	$825.590
Corporation License Tax	$87.901	$103.320	$123.315	$128.179
Total	**$805.735**	**$842.081**	**$905.206**	**$953.769**
Individual Income & Corp. License Tax Grov		**4.51%**	**7.50%**	**5.36%**
SB 372 growth "Trigger" (4% growth)		Yes	**Yes**	Yes

5. This fiscal note assumes that the trigger is met and certified on August 1, 2012, and will apply in TY 2013.

<u>Class 8 (Business Equipment) Taxable Value Reduction</u>

6. The TY 2010 taxable value of all class 8 property in the DOR property data base was used to model the impact of SB 372 tax rate reductions and increase in tax brackets. The current TY 2010 taxable value of class 8 property is $176,107,343.
7. The TY 2010 taxable value of class 8 property was estimated for each level prescribed in the SB 372 as amended resulting in the following schedule of class 8 property taxable values (in TY 2010 values).

Modeled Class 8 Taxable Value Change SB 372 as Amended in Senate Committee

Schedule	**Threshold and Tax rate (No tax if value less than $20,000)**	**TY 2010 Taxable Value**	**Change from Current Law**	**Increment to Increment**
Current Law		$176,107,343	0%	$0
SB 372	First $2 Million @ 2.0%	$149,576,285	-15.1%	-15.1%
Increment	First $3 Million @ 1.5%	$133,583,061	-24.1%	-10.7%

8. The current law and SB 372 as amended (TY 2010) schedule of taxable value are projected using HJR 2 growth rates for TY 2011, TY 2012, and TY 2013 and the Office of Budget and Program Planning (OBPP) growth rates for TY 2014 and TY 2015. The growth rates are as follows.

HJR 2 Average Growth Rates for Property Tax Class 8 and Class 12 Revenue Effects

Property Type	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
Class 8	7.50%	5.00%	5.00%	5.00%
Class 12	2.10%	1.20%	2.10%	2.10%

9. Taxable value change is calculated by subtracting current law taxable value from SB 372 (as amended) estimated taxable value.

Change in Class 8 Taxable Value SB 372 as Amended in Senate Committee				
Tax Year	**TY 2012**	**TY 2013**	**TY 2014**	**TY 2015**
Class 8 Taxable Value (Current Law)	198,781,163	208,720,221	219,156,232	230,114,044
Class 8 Taxable Value (SB 372)	168,834,231	158,320,974	166,237,023	174,548,874
Difference (SB 372 - Current)	**(29,946,932)**	**(50,399,247)**	**(52,919,210)**	**(55,565,170)**
% Difference	-15.07%	-24.15%	-24.15%	-24.15%

10. The initial effect of SB 372 is to lower the tax rate to 2.0% on the first $2 million in market value of property. Additionally, it is assumed that the FY 2012 trigger is met, reducing the tax rate to 1.5% in TY 2013. Compared to current law, SB 372 as amended reduces the taxable value of class 8 property in TY 2012 and in TY 2013 after which the rate and the threshold will remain constant, resulting in approximately a 24.15% reduction in taxable value.

Class 12 Taxable Value Reduction (Railroad and Airline Property)

11. The class 12 (railroad and airline property) tax rate is calculated based on the statewide average tax rate for all other commercial and industrial property in the state (class 4 commercial property, and classes 8, 9, 13, 14, 15, and 16). The reduction in class 8 taxable value under SB 372 as amended, results in a decrease in the weighted average tax rate for class 12. The TY 2010 tax rate for class 12 property was 3.40%. Recalculating the tax rate with the reduced taxable values for class 8 property resulting from this bill would decrease the class 12 tax rate. This effect starts in TY 2013 (FY 2014) as the calculation is based on the prior tax year's weighted average. The effect is presented in the following table:

Change in Class 12 Taxable Value Due to Class 8 Reductions in SB 372 as Amended in Senate Committee				
Fiscal Year	**TY 2012**	**TY 2013**	**TY 2014**	**TY 2015**
Class 12 Market Value	$1,566,561,450	$1,585,360,187	$1,618,652,751	$1,652,644,459
Current Law Tax Rates	3.38%	3.33%	3.28%	3.26%
Tax Rate with HB 372 Class 8 Changes	3.38%	3.32%	3.19%	3.16%
Class 12 Taxable Value (Current Law)	$52,949,777	$52,792,494	$53,094,233	$53,879,673
Class 12 Taxable Value (SB 372)	$52,949,777	$52,633,958	$51,659,254	$52,261,665
Class 12 Taxable Value Difference	**$0**	**($158,536)**	**($1,434,979)**	**($1,618,008)**
% Difference (Bill - Current)	0.00%	-0.30%	-2.70%	-3.00%

Rail Car Tax Revenue Impact

12. The reduction in the class 12 tax rate reduces the state general fund tax on railroad cars. The rolling stock of railroad car companies is taxed based on the Montana allocated value of the national railroad car fleet and the class 12 property tax rate. The average statewide commercial and industrial mill rate is applied to this taxable value. The impact of the change in the class 12 tax rate, based on the HJR 2 and OBPP assumptions for the growth in Montana allocated value and mill rates, is presented below:

Change in Rail Car Tax under SB 372 as Amended in Senate Committee				
	FY 2012	**FY 2013**	**FY 2014**	**FY 2015**
Montana Allocated Value	$118,886,000	$122,929,000	$123,485,000	$124,041,000
Current Law Class 12 Tax Rate	3.38%	3.33%	3.28%	3.26%
Class 12 Tax Rate SB 372	3.38%	3.32%	3.19%	3.16%
Current Law Taxable Value	4,018,347	4,093,536	4,050,493	4,043,997
Taxable Value under SB 372	4,018,347	4,081,243	3,941,020	3,922,555
Taxable Value Difference	-	(12,293)	(109,473)	(121,441)
Statewide Mills	521.50	526.30	531.26	536.22
Revenue Change	**$0**	**($6,470)**	**($58,159)**	**($65,120)**

<u>*Projection of State Property Tax Revenue Impact*</u>

13. Based on preceding taxable value reduction estimates for class 8 property and class 12 property and the statewide average mill rates by class, the anticipated reduction in state revenue under SB 372 as amended for FY 2012 through FY 2015 is presented in the following table.

Change in State Property Tax Revenue under SB 372 as Amended in Senate Committee					
Change in Taxable Value		**TY 2012**	**TY 2013**	**TY 2014**	**TY 2015**
Class 8		(29,946,932)	(50,399,247)	(52,919,210)	(55,565,170)
Class 12		0	(158,536)	(1,434,979)	(1,618,008)
Revenue (FY)	**Mills**	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
General Fund					
Class 8	95.82	($1,262,587)	($3,731,801)	($4,935,500)	($5,182,274)
Class 12	95.82	$0	$0	($15,191)	($137,500)
Total		**($1,262,587)**	**($3,731,801)**	**($4,950,690)**	**($5,319,774)**
State Special Revenue					
Class 8	6.00	($79,060)	($233,676)	($309,048)	($324,501)
Class 12	6.00	$0	$0	($951)	($8,610)
Total		**($79,060)**	**($233,676)**	**($309,999)**	**($333,110)**

14. These projections are adjusted for the fiscal year receipt of property tax. Most property taxes are paid in November and May of the fiscal year following assessment. However, under the provisions of 15-16-119, MCA, owners of personal property that is not liened-to-real property (Class 8) pay property taxes 30-days after assessments are mailed in March. This means that not liened-to-real property taxes are paid in the fiscal year they are billed. In TY 2010, class 8 property not liened-to-real property made up 44.0% of the total value of TY 2010 class 8 property (FY 2010). It further means that 56.0% of TY 2010 property taxes are paid in FY 2011.
15. This bill would reduce class 8 taxable values starting in TY 2012. The impact would start in FY 2012 for personal property not liened-to-real property (44% of TY 2012 property), and in FY 2013 for all property.

<u>*Business Tax Revenue Increase*</u>

16. With lower property taxes, businesses will have lower property tax expenses to deduct in calculating taxable net revenue. The estimated reduction in net property tax is calculated based on the state and local property tax reductions estimated in this fiscal note.

17. Corporations that do business in Montana and other states are required to report their Montana property on their corporation license tax returns. Of this property, 66.65% was reported by corporations that had positive taxable income. It is assumed that the same proportion of total business property is owned by businesses with positive net income.
18. Each calendar year, the reduction in business expenses is half of the reduction in property tax for profitable businesses for the same numbered fiscal year plus half of the reduction for the next fiscal year.
19. The corporation license tax rate is 6.75%. It is assumed that the average marginal tax rate on business income reported on individual income tax returns is also 6.75%.
20. Businesses frequently use the option for an extended deadline for filing tax returns. Because of this, the changes in tax liability will be reported on tax returns filed over the course of the following calendar year, with half of the change coming in the fiscal year including the last half of the tax year and half coming in the next fiscal year. The result is presented in the following table:

Estimated Business Tax Revenue Increase Under SB 372
as Amended in Senate Committee

Property Tax Reduction		**TY 2012**	**TY 2013**	**TY 2014**
State		(2,653,562)	(4,613,083)	(5,456,787)
Local Government		(5,567,997)	(9,678,917)	(11,442,347)
Schools		(5,540,372)	(9,631,056)	(11,387,180)
TIFs		(428,575)	(743,753)	(868,220)
Decrease in Property Tax Liability		($14,190,505)	($24,666,809)	($29,154,534)
	FY 2012	**FY 2013**	**FY 2014**	**FY 2015**
Increase in Business Taxes	**$0**	**$319,207**	**$871,707**	**$1,206,567**

21. This bill provides for reimbursements to school districts (through school block grants) to local governments, tax increment financing (TIFs) districts (through entitlement share payments), and to the university system for 6 mill levy revenue losses due to the elimination of taxable value under this bill. The total property tax revenue losses are estimated using the taxable value change and the statewide weighted average mills for each level of government. Note that taxable value reductions are presented on a tax year basis, the revenue reductions are presented by fiscal year of impact. TIF statewide taxable value is approximately 3.15% of all statewide class 8 taxable value; there is no class 12 TIF taxable value. These revenue reductions before reimbursements are estimated and presented in the following table.

Net Impact on Local Government Taxable Value and Property Tax Revenue - SB 372 as Amended in Senate Committee

Change in Taxable Value		TY 2012	TY 2013	TY 2014	TY 2015
Class 8		(29,946,932)	(50,399,247)	(52,919,210)	(55,565,170)
Class 12		0	(158,536)	(1,434,979)	(1,618,008)
Taxable Value Reduction		**(29,946,932)**	**(50,557,783)**	**(54,354,189)**	**(57,183,178)**
Property Tax (FY) Revenue Reductio	**Mills**	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
School Districts					
Class 8 Property	212.59	($2,801,224)	($8,279,520)	($10,950,092)	($11,497,597)
Class 12 property	205.00	$0	$0	($32,500)	($294,171)
Total School Districts		**($2,801,224)**	**($8,279,520)**	**($10,982,592)**	**($11,791,768)**
Local Governments					
Class 8 Property	213.65	($2,815,191)	($8,320,802)	($11,004,691)	($11,554,925)
Class 12 property	204.00	$0	$0	($32,341)	($292,736)
Total Local Governments		**($2,815,191)**	**($8,320,802)**	**($11,037,032)**	**($11,847,661)**
Tax Increment Districts					
Taxable Value in TIFs (3.15% of Class 8)		($943,328)	($1,587,576)	($1,666,955)	($1,750,303)
Class 8 Property Revenue	522.06	**($216,689)**	**($640,462)**	**($847,044)**	**($889,396)**
Total Local Juristiction Revenue Reduction		**($5,833,104)**	**($17,240,784)**	**($22,866,668)**	**($24,528,825)**

22. The bill provides for reimbursement at 90% of the direct revenue loss to each level of government. The following table presents the estimated reimbursement for each level of government and the designated reimbursement mechanism:

Reimbursements for the Change in Taxable Value Under SB 372 as Amended in Senate Committee

Reimbursement Jurisdiction	FY 2012	FY 2013	FY 2014	FY 2015
Reimbursement Rate	90%	90%	90%	90%
School Districts				
Increase in School Block Grants	**$2,521,102**	**$7,451,568**	**$9,884,333**	**$10,612,591**
Local Governments				
Increase in Entitlement Share Payments	**$2,533,672**	**$7,488,722**	**$9,933,329**	**$10,662,895**
Tax Increment Districts				
Increase in Entitlement Share Payments	**$195,020**	**$576,416**	**$762,340**	**$800,456**
University 6 mill Revenue				
Reimbursement to OCHE	**$71,154**	**$210,308**	**$278,999**	**$299,799**
Total Property Tax Reimbursements	**$5,320,947**	**$15,727,014**	**$20,859,001**	**$22,375,742**

23. SB 372 has coordinating language with proposed HB 26 which amends 15-10-420(7), MCA, which prevents local jurisdictions from raising mills for the part of the tax base lost to SB 372 that is reimbursed.

Department of Revenue Administrative Expenses

24. Because SB 372 reduces class 8 property tax rate on a portion of class 8 property, the department will need to make programming changes in the property tax database system. The department assumes these changes will cost $14,850 in FY 2012.

Office of Public Instruction

25. The decrease in property tax revenues due to this bill for not liened-to-real property in FY 2012 does not have a Guaranteed Tax Base Aid (GTB) effect on K-12 schools because GTB would have been determined before the bill is effective in FY 2012.
26. The loss of taxable value occurs in annual steps in TY 2012 through TY 2013. There would be GTB cost adjustments for FY 2013 through FY 2015 related to this bill. These GTB costs are offset because the reimbursement payments would be considered non-levy revenue for school budgeting purposes. Non-levy revenues are considered prior to GTB calculation in school budgeting. Therefore, the reimbursement goes into school district base, with the net effect of reducing GTB costs relative to current law.
27. There would also be countywide retirement GTB effects. These are assumed to be proportionate (at FY 2010 levels) with respect to statewide GTB payments ($30 million retirement GTB cost/$140 million GTB costs) GTB costs are presented in the following table:

Net GTB Impact from Loss of Taxable Value and Property Tax Base Reimbursements under SB 372 as Amended in Senate Committee

	FY 2012	FY 2013	FY 2014	FY 2015
GTB Costs	$0	594,571	995,006	(93,019)
Reimbursement Effect	(576,910)	(2,764,880)	(2,764,880)	(2,764,880)
Net GTB effects	($576,910)	($2,170,308)	($1,769,874)	($2,857,898)
Retirement GTB Estimate		($465,066)	($379,259)	($612,407)

Secretary of State

28. There will be minimal cost for postage and administrative duties to make the tribal notifications required by the bill. Since the Office of the Secretary of State does not receive any general fund appropriations, the costs will be covered from the agency enterprise fund.

Fiscal Impact:	**FY 2012 Difference**	**FY 2013 Difference**	**FY 2014 Difference**	**FY 2015 Difference**
Department of Revenue				
Expenditures:				
Operating Expenses	$14,850	$0	$0	$0
Transfers:				
Local Governments	$2,533,672	$7,488,722	$9,933,329	$10,662,895
Tax Increment Districts	$195,020	$576,416	$762,340	$800,456
University System (OCHE)	$71,154	$210,308	$278,999	$299,799
TOTAL Expenditures	$2,814,696	$8,275,446	$10,974,668	$11,763,151
Funding of Expenditures:				
General Fund (01)	$2,814,696	$8,275,446	$10,974,668	$11,763,151
TOTAL Funding of Exp.	$2,814,696	$8,275,446	$10,974,668	$11,763,151
Revenues:				
General Fund - Property Tax	($1,262,587)	($3,731,801)	($4,950,690)	($5,319,774)
General Fund - Business Income Ta	$0	$319,207	$871,707	$1,206,567
General Fund - Rail Car Tax	-	($6,470)	($58,159)	($65,120)
SSR(02) - Property Tax	($79,060)	($233,676)	($309,999)	($333,110)
TOTAL Revenues	($1,341,646)	($3,652,740)	($4,447,142)	($4,511,437)
Office of Public Instruction:				
Expenditures:				
Transfers:				
Local Assistance (All Funds)	$2,521,102	$7,451,568	$9,884,333	$10,612,591
Local Assistance (GTB)	($576,910)	($2,170,308)	($1,769,874)	($2,857,898)
Local Assistance (Co. Retirement)	$0	($465,066)	($379,259)	($612,407)
TOTAL Expenditures	$1,944,192	$4,816,193	$7,735,201	$7,142,286
Funding of Expenditures:				
General Fund (01)	$1,944,192	$4,816,193	$7,735,201	$7,142,286
TOTAL Funding of Exp.	$1,944,192	$4,816,193	$7,735,201	$7,142,286
Net Impact to Fund Balance (Revenue minus Funding of Expenditures):				
General Fund (01)	($6,021,474)	($16,510,703)	($22,847,011)	($23,083,763)
State Special Revenue (02)	($79,060)	($233,676)	($309,999)	($333,110)

Effect on County or Other Local Revenues or Expenditures:

1. The 10% unreimbursed decrease in local school revenue and local government revenue will lead to tax shifts as tax obligation is passed from class 8 property and class 12 property to other property classifications. TIFs would see shifts which would be offset by local and school mills. TIFs would share in the 95 mill revenue reductions. The unreimbursed property tax revenue – before tax shifts – are estimated in the following table:

Unreimbursed Portion of Taxable Value Reduction Under SB 372 as Amended in Senate Committee				
Reimbursement Jurisdiction	**FY 2012**	**FY 2013**	**FY 2014**	**FY 2015**
School Districts	$280,122	$827,952	$1,098,259	$1,179,177
Local Governments	$281,519	$832,080	$1,103,703	$1,184,766
Tax Increment Districts	$21,669	$64,046	$84,704	$88,940
Direct Property Tax Foregone	**$583,310**	**$1,724,078**	**$2,286,667**	**$2,452,882**

Long-Term Impacts:

1. After completing the schedule of incremental rate reductions and bracket increases, SB 372 as amended removes approximately 24.15% of class 8 taxable value and 3% of class 12 taxable value from the taxation system.

Technical Notes:

Department of Revenue

1. Page 7, line 24, Coordination Section: speaks to the amended versions of HB 26.
2. SB 372 provides for an exemption of class 8 business property, for example a forklift, but does not provide an exemption for the same type of property that happens to be in a different tax class; for example a class 9 centrally assessed forklift owned by a electric power company or class 12 forklift owned by a railroad. Treating the same property differently could create equity issues and potentially lead to litigation.
3. The bill title references corporation license tax and the language found in section 1 at 15-6-138(4)(a), MCA, calls it corporation income tax. The bill indicates the change in rates applies to measuring revenues collected on corporation income tax in the body of SB 372 versus corporation license tax as appears in the title of SB 372. HJR 2 presents the Legislature's official forecast of individual income tax and corporation license tax. If the intent of the bill is to adjust class 8 tax rates based on the corporate income tax then it is likely the measure will be limited to the changes in collections of individual income tax
4. The language on page 3 refers to subsection (3)(A) (uppercase "A") in numerous places in subsections (3) and (4). The reference should be to lowercase (a).

Office of Public Instruction

5. SB 403 caps school block grant funding for some districts. This may conflict with the reimbursements in SB 372 through school block grants.

Sponsor's Initials | *Date* | *Budget Director's Initials* | *Date*